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DIRECTORATE OF INTELLIGENCE

20 May 1987

Jordan: Balance of Payments Trends and Prospects* [redacted] 25X1

Summary

Jordan will have to cope with a substantial worsening of its balance of payments position during the remainder of the 1980s. Resource-poor Jordan will remain heavily dependent on imports during a time when foreign markets for its major exports will remain sluggish. We do not believe Arab financial aid and remittances of expatriate workers will cover the impending trade deficits. As a result, Amman will have to increase foreign borrowing--and add to its already mounting foreign debt--if it is to maintain current import levels without depleting already dangerously low foreign exchange reserves. At the same time, balance of payment shortfalls will translate directly into increased deficits for the domestic budget.

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A major cause of Jordan's balance of payment difficulties is a decline in Arab aid promised Jordan under the 1978 Baghdad Accord. Last year, Baghdad payments--Jordan's third-most important source of income--fell to $577 million from $667 million in 1985 and a peak of $1.2 billion in 1981, according to the US Embassies in Amman and Doha. Only Saudi Arabia continues to honor its original pledge. The regional recession also has translated into stagnating worker remittances that are Jordan's most important foreign exchange earner, as job opportunities for Jordanians in the Persian Gulf have tapered off.

Cheaper prices for oil and fuel imports--especially in 1986 when the oil price fell by almost half to $15 per barrel--have helped offset the slowdown in worker remittances and the dropoff in Arab grants. We estimate real savings of roughly $250 million on the oil bill accounted for about 40 percent of the drop in import costs from $3.0 billion in 1983 to $2.4 billion last year. 25X1
Reduced imports, especially of project-related capital goods,

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*This memorandum was prepared by [redacted] the Israel-Jordan-PLO Branch, Arab-Israeli Division, Office of Near Eastern and South Asian Analysis at the request of Frank Kerber of NEA/ARN State Department. Information as of 20 May was used in its preparation. Questions and comments should be addressed to Chief, Arab-Israeli Division [redacted] 25X1 25X1

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have helped gradually improve the current account deficit that fell from $387 million to about $75 million over the same period. Nevertheless, Jordan has been forced to increase foreign borrowing and to draw down its foreign exchange reserves to cover the current account deficit.

Intractable Trade Deficits*

We believe Jordan lacks the necessary self-sufficiency and political will to make additional deep cuts in import spending. Lacking key resources of its own, Jordan remains heavily dependent on imports of food, raw materials, and oil to support its economy. The cost of foreign oil, which accounts for roughly 15 percent of total imports, is likely to increase this year as a result of an expected 20 percent jump in the average price of OPEC crude. Food accounts for about 13 percent of imports; while other consumer goods make up over two-thirds of the import bill.

Amman's new restrictive trade legislation is unlikely to have an appreciable effect on reducing import spending. The government last February approved tariff regulations that raise customs duties on a wide variety of luxury consumer goods, including alcohol, ready-made clothes, and selected food items. Tariffs on most alcoholic beverages and clothing have at least doubled. These measures are expected to reduce consumption of these items as well as earn the government about $50 million annually, according to the US Embassy. At the same time, Jordan has reduced customs duties on essential imports for domestic industry. The anticipated larger oil bill, however, probably will offset most of the additional revenue Amman expects to generate from its new import tariffs.

In our judgment, Amman is unlikely to provoke popular resentment by enacting measures that would sharply cut imports of consumer goods. Any significant reduction in the standard of living would not go over well in a society that has become accustomed to Western material values during the relative boom years of 1970s. Moreover, Jordan has embarked on an ambitious five-year development program and will be reluctant to curtail project spending to the point that it threatens the politically sensitive objectives of increasing employment in Jordan and securing Palestinian support in the Israeli-occupied West Bank.

Export performance is unlikely to be substantially better by 1990. Jordan will be hard-pressed to maintain sales of phosphates and fertilizers which account for roughly 40 percent of export earnings. World prices for phosphates, which already have fallen from $42 per metric ton in 1982 to $34 last year, probably will remain depressed. Jordan also probably will not succeed in its attempt to offset the impact of the weak world commodity market by aggressively boosting export volume as it did

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*Our forecasts assume no clear victor emerges from the Iran-Iraq War.

last year when it sold 5.2 million tons of phosphates, a 12.8 percent increase over 1985. Stiffer competition, especially from Morocco, will probably force Jordan to offer generous credit terms or even to cut phosphate prices just to maintain its market share.

Jordan probably will concentrate on Eastern Europe for new phosphate markets in part to avoid the price retaliation that would result from an all-out trade war with Morocco. Eastern European countries already take over two-thirds of Jordan's phosphates exports. Most of Jordan's trade with Eastern Europe, however, is based on counterpurchase agreements that require Amman to accept inferior goods and services-- rather than hard currency--in exchange for its phosphates.

As a result of weak demand for Jordan's major exports, especially phosphates, and continued heavy reliance on imports we believe Amman will be saddled with annual trade deficits of around $1.7-1.9 billion over the next three years.

Current Account Shortfall to Continue

Jordan can expect less assistance from its Arab benefactors through the remainder of the 1980s. Beginning this year, Oman discontinued its Baghdad payments that amounted to $115 million in 1986 [redacted] Kuwait 25X1 also has suspended payments that amounted to roughly $74 million last year. Amman hopes that Kuwait will provide oil and chemical products worth $30-40 million this year. With financial problems of their own, Saudi Arabia and Qatar have rebuffed Jordanian requests for increased aid. [redacted] 25X1 Assuming that only Saudi Arabia, the UAE, and Qatar provide Baghdad grants at last year's levels--and Kuwait does come through with the aid-in-kind--Jordan will receive $460 million in Arab aid in 1987. Continued aid becomes problematic beyond 1988 when the Baghdad payment agreement expires.

Worker remittances are likely to decline slowly over the next several years. Job opportunities, especially for skilled labor, probably will continue to dwindle in the Gulf states where nearly all Jordanian expatriate workers found employment. Last year only 4,000 Jordanians found jobs abroad, compared with 5,600 in 1985 and over 11,800 in 1983 according to the US Embassy in Amman. By 1990, Jordan may have to cope with a net return of its overseas workers. Those Jordanians who are able to keep their jobs probably will have to accept lower wages as employing countries cut their wage bills and hire less skilled, and cheaper, workers. The average wage in Saudi Arabia, for example, is down 20-30 percent over last year, according to the US Embassy in Riyadh, and new hires are offered up to 50 percent less.

Tourist earnings also will remain in the doldrums. The number of Arab travelers to Jordan has declined sharply, according to the Embassy, reflecting lower incomes in the region and the more expensive Jordanian currency. Fear of terrorism causes Western tourists increasingly to avoid the region.

As a result, we believe Jordan will experience chronic current account deficits during the remainder of the decade even if imports are held roughly at the current level. The current account deficit is likely to rise to about $150 million this year from an estimated $75 million in 1986.

<u>More Borrowing Ahead</u>

Jordan will not be able to tap foreign exchange holdings to cover this shortfall. Foreign exchange reserves already have plummeted from over $1 billion in 1980 to $414 million last year, and by March 1987 had dropped to $212 million--equivalent to less than two month's imports at current rates. Although Amman has eliminated several of the major causes of the decline--including financing reexports to Iraq--it still must pay off other claims that threaten to deplete reserves. Amman, for example, must make payments on its military debt that as of February included $52 million in total arrearages owed the United States.

Jordan now has the added burden of settling accounts for Saudi oil purchases made in the last half of 1985. Riyadh is insisting that Amman pay $195 million for oil delivered through the Saudi-owned Tapline according to the US Embassy in Amman. [redacted] 25X1 Amman, however, has made no progress on repaying this debt, and has fallen behind on payments for new oil deliveries, according to the US Embassy.

Jordan, therefore, will need to turn to increased foreign commercial borrowing in order to avoid substantial cuts in imports. The kingdom has roughly $1.2 billion in undisbursed official loans, but most represent loans specifically linked to previously curtailed development programs. As a result, Jordan cannot draw down any unused loans for discretionary balance of payments relief.

To help compensate for the loss in Arab aid, Jordan probably will rely more heavily on internationally-syndicated bank loans--offered at higher commercial rates-- to help finance its foreign payments deficits. Jordan signed a seven-year syndicated loan agreement in March with the Arab Bank and 19 other participating banks for $150 million. Reflecting the image of Jordan as stable and creditworthy, the recent syndicated commercial loan was oversubscribed at the underwriting stage, according to the press.

Nevertheless, a continued trend of heavy commercial borrowing, will test Jordan's ability to service a foreign debt

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which has increased from $1.7 billion in 1982 to nearly $3 billion in September 1986. Jordan's debt-service ratio--a measure of how much of its foreign exchange earning from exports and worker remittances must be used to make annual payments--has jumped from about 15 percent in 1983 to 27 percent. Moreover, Jordan's share of outstanding debt to commercial lenders has doubled since 1982 to about 34 percent last year according to official statistics. Because these loans often are at higher interest rates, they have been a major contributor to the sharp increase in debt-service payments.

Sizable Budget Deficits

Jordan's balance of payments difficulties will have a direct impact on the domestic budget. In contrast to the expansionary budget last year when spending grew nearly 25 percent over 1985, planned expenditures this year show less than a 2 percent increase, according to the US Embassy in Amman.

The government also has taken a number of steps to cut budget expenditures, according to the Jordanian press, that include:

--Suspension of exceptional promotions and new appointments as well as cancellation of overtime allowances;

--Reduction of the allocation for water, electricity, and various supplies by 10 percent;

--Limitation on foreign travel and research spending; and

--Suspension of spending on several construction projects, including some water and sewerage development and the Al-Hasan sports city in the northern city of Irbid.

Amman expects these measures will save about $60 million. Much of these savings, however, will be washed out by the government's recent decision to provide about $45 million to help bail out municipalities that borrowed heavily for projects in the five-year development plan.

Despite the austerity measures, we believe Jordan is unlikely to hold the overall budget deficit to the projected $190 million. Realized revenue from foreign loans and grants--especially Arab aid--will fall well short of the anticipated level of about $600 million. Moreover, the economy is unlikely to grow rapidly enough to sustain the sharp increase in domestic revenues forecast in the budget. As a result, we believe the

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budget deficit will be close to last year's $634 million. Without cutting spending, the government will have to finance the balance of the deficit through a combination of domestic borrowing and increases in the money supply.

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JORDAN: BALANCE OF PAYMENTS

(Millions US $)

	1983	1984	1985	1986[1]	1987[2]	1988[2]	1989[2]
TRADE BALANCE	-2,460.3	-2,032.7	-1,938.0	-1,730.8	-1,740.0	-1,810.0	-1,880.0
EXPORTS	580.4	757.0	788.8	684.4	710.0	740.0	770.0
IMPORTS	3,040.7	2,789.7	2,726.8	2,415.2	2,450.0	2,500.0	2,650.0
SERVICES	1,254.4	1,030.3	879.9	937.5	989.0	967.0	914.0
WORKER REMMITANCES	909.8	983.0	786.6	1,016.0	1,060.0	1,050.0	1,000.0
TOURISM	139.5	69.7	95.8	103.5	108.0	112.0	117.0
INVESTMENT INCOME	45.7	-60.6	-88.8	-138.3	-134.0	-145.0	-148.0
OTHER	159.4	38.2	86.3	-43.7	-46.0	-48.0	-49.0
GRANTS	818.0	735.8	806.4	717.9	600.0	605.0	650.0
BAGHDAD PACT	711.9	604.6	667.0	577.0	460.0	460.0	400.0[3]
OTHER	106.1	131.2	139.4	140.9	140.0	145.0	150.0
CURRENT ACCOUNT	-387.9	-266.6	-251.7	-75.4	-151.0	-186.0	-310.0

1 Estimate
2 Forecast
3 Baghdad payments agreement expires in 1988, but we assume some grants--particularly from Saudi Arabia--will continue on an ad hoc basis.

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